Ernst & Young Ltd
100 Willis St, Wellington 6011
P O Box 490, Wellington 6140

Tel: +64 4 499 4888
Fax: +64 4 495 7400
ey.com/nz

Building a better working world

GST on low-value imported goods
C/- Deputy Commissioner Policy and Strategy
Inland Revenue Department
PO Box 2198
Wellington 6140

29 June 2018

Email: policy.webmaster@ird.govt.nz

Dear Cath

Submission on government discussion document *GST on low-value imported goods: An offshore supplier registration system*

We refer to the proposals contained in the government discussion document, *GST on low-value imported goods: An offshore supplier registration system* ("the DD") and Inland Revenue's associated memorandum *GST on low-value imported goods proposals: Scope of the marketplace rules, double taxation issues and valuation methods for determining whether goods are above or below the proposed $400 threshold* ("IRD memo"). We appreciate the opportunity to comment on the proposals.

1 Summary of main comments

1.1 The proposals address a material, longstanding hole in the GST base and in principle we support charging GST on low-value imported goods. The proposals should improve the tax neutrality between imported and domestically retailed low-value goods, without imposing major disruption on consumers importing goods.

1.2 However, aspects of the proposals require further consideration to ensure the rules are workable in practice and do not result in unnecessary compliance costs. Our main comments are summarised below, followed by a more detailed analysis:

- We believe it will be hard to enforce compliance with the proposed rules and there is a risk that many businesses will not comply.
- The ability of Customs to administer the $400 threshold will be crucial to the success of the proposals.
- The option of collecting GST between the point of sale and delivery should be further explored for possible implementation in the medium term – the current proposals are likely to provide an interim solution only.
- A post-implementation review should be carried out after no more than five years following enactment of the proposals.
- In relation to double taxation:
  - The ideal solution would be to stop double taxation from occurring in the first place. Could there be a Customs hotline or online portal to allow the supplier/consumer to prevent double taxation before the goods arrive?
  - If preventing double taxation is not possible, the question of how the consumer can provide appropriate evidence as to GST already collected needs to be explored and appropriately resolved before the proposals are implemented.
  - Requiring exchange rate information on import entry documentation is likely to place additional compliance requirements on Customs when the variances may not be material. In addition, a special system for New Zealand may not be realistic. Instead,

if Customs has evidence that GST has been paid, could it be allowed not to enforce the $400 threshold for those goods rather than check exchange rate calculations?

- The "reasonable belief" exception is too subjective and will be difficult for Inland Revenue to enforce.

- In relation to electronic marketplaces ("EMPs"):
  - We agree with treating the marketplace as the default supplier of the goods, however there is a risk that some EMPs may be reluctant to supply into the New Zealand market as a result of the new rules, similar to the experience in Australia.
  - Deeming the EMP operator to be the supplier in relation to supplies made in New Zealand (on which GST is working well) seems unnecessarily complex. The alternative option of deeming the EMP operator to be the supplier only if the vendor is based outside New Zealand is also not without issues.
  - We do not support a carve-out for EMPs through which predominantly domestic supplies are made as it would require complex tracking and assumes an unchanging business model in a fast-moving space.
- Other matters:
  - Identifying business-to-business supplies – further consideration should be given to how offshore suppliers can accurately identify GST-registered businesses, particularly in the absence of a public register for GST-registered businesses.
  - Joint registration system – such a system is likely to be unworkable in the foreseeable future. Instead, the Government should focus its resources on data matching and information sharing with the Australian Tax Office.

2 Compliance issues

2.1 We question the accuracy of the statement at paragraph 5.1 of the DD that "It is expected that most offshore suppliers of low-value goods would comply with the rules..."

2.2 The proposals are dependant on voluntary compliance from many non-resident vendors (including small businesses) and marketplaces with no presence in New Zealand. Ensuring compliance will require offshore enforcement against each of these businesses in every country in which they operate.

2.3 There is a risk many businesses will not comply with the proposals, and it will be difficult to identify all instances of non-compliance and impose consequences on those who do not comply. For all except the biggest suppliers, the collection of GST will in substance be voluntary.

3 Scope and thresholds

3.1 The proposals appear to be a partial stop-gap – goods valued at $400 or less from offshore suppliers whose total supplies of goods and services to New Zealand consumers do not exceed $60,000 a year would remain outside the base.

3.2 As stated at paragraph 3.3 of the DD, under the proposals the taxing point for imported goods valued at or below $400 would shift to the point of sale. We agree that for a system of this nature to work the low-value threshold must be as low as possible in order to keep revenue losses to a minimum.

3.3 However, the ability of Customs to administer the $400 threshold will be crucial to the success of the proposals. We note the equivalent rules in Australia have a threshold of AUD 1,000. Careful consideration needs to be given as to whether the $400 threshold is workable, including:

- Is a lower threshold possible?
- What changes can Customs consider to its systems to ensure administering the $400 threshold (or a lower one if possible) is cost effective?
- Is Customs prepared to take a loss on cost recovery to keep the threshold low?

4 Will reform be temporary only?

4.1 Paragraph 1.9 of the DD refers to the option of collecting GST between the point of sale and delivery, where courier companies and New Zealand Post would collect GST, tariffs and cost recovery charges. However, the DD defers to the Tax Working Group's view, supported by the findings of the Australian Productivity Commission, that this option is not feasible in the short-term.

4.2 In our view:

- Requiring the delivery agent to collect GST could be explored further, as it places the liability for assessing and collecting GST on entities within New Zealand and does not exempt goods from suppliers below the registration threshold. Using information technologies to monitor enforcement or facilitate collection seems desirable. Care would need to be taken to ensure that unreasonable compliance costs were not placed on the delivery agent.
- Such an approach seems likely to achieve higher compliance and collection rates but at the cost of a higher administrative and compliance burden.
- Currently, the existing paper-based declaration processes still in operation for most goods sent by international mail would make this approach too costly. We note the Australian Productivity Commission has stated that the Universal Postal Union is currently promoting an upgrade to a system involving electronic data transmission, but not until 2023[1].

4.3 We believe the option of collecting GST between the point of sale and delivery should be further explored for possible implementation in the medium term once international postal agreements catch-up. The current proposals are likely to provide an interim solution only.

5 Post-implementation review

5.1 We recommend a post-implementation review be carried out after no more than five years following enactment of the proposals. This review should consider whether the proposals are working as intended and whether it is desirable to change to a model which collects GST between the point of sale and delivery. In particular, this review should look at:

- Whether offshore suppliers are complying with their obligations to collect GST on low-value imported goods.
- Technological changes and whether international mail has upgraded to a system involving electronic data transmission. This consideration would be consistent with the Tax Working Group's comment in its Letter to Ministers where the Group states[2]:

> *"...the Group recommends that the Government continue to review the options to collect GST between the point of sale and delivery and after delivery following implementation of an offshore supplier registration model. This continued review should consider whether the feasibility issues with these options can be overcome as technology and data sharing improvements occur."*

[1] Australian Productivity Commission Inquiry Report *Collection Models for GST on Low Value Imported Goods*, 31 October 2017, page 8. See http://www.pc.gov.au/inquiries/completed/collection-models/report (last accessed 28 June 2018).
[2] See http://taxpolicy.ird.govt.nz/sites/default/files/news/2018-05-01-dd-gst-low-value-goods-twg-letter.pdf (last accessed 28 June 2018).

6 Double taxation

Further exploration of possible solutions necessary

6.1 As noted in the DD and elaborated on in the IRD memo, the proposals may result in the consumer being subject to double taxation in certain circumstances, such as where the consumer has purchased multiple goods which are packaged together in the same consignment. While the IRD memo contains more discussion than the DD, both documents are light on details regarding how double taxation will be prevented.

6.2 Paragraph 3.17 of the DD suggests the consumer would need to provide Customs with appropriate evidence that GST had already been paid on the low-value goods portion in the consignment before they can obtain a refund of the double taxation. The IRD memo suggests the vendor or transporter should be able to indicate on the import entry documentation the items in the consignment on which GST has already been collected. In the absence of such notification, the IRD memo suggests the consumer will need to provide Customs with a receipt or invoice showing GST has already been charged on some or all of the goods.

6.3 In our view, it is unrealistic to expect the vendor or transporter to provide an indication as to GST on the import entry documentation. Vendors, transporters and, more specifically, customs brokers are likely to be reluctant to move away from the established norm and accuracy / compliance may be less than desirable.

6.4 We agree with the concerns at page 8 of the IRD memo that consumers may not be aware double taxation has occurred, or may not wish to incur the compliance costs associated with obtaining a relatively small refund. The ideal solution would be one where double taxation does not occur in the first place. Could there be a Customs hotline or online portal to allow the consumer to prevent double taxation before the goods arrive or the supplier to confirm GST has been charged?

6.5 If preventing double taxation is not possible, we agree with the IRD memo that consumers need to be made aware of the potential for double taxation whenever they have paid GST to Customs and that obtaining a refund should be as painless as possible. The question of how the consumer can provide appropriate evidence as to GST already collected needs to be explored and appropriately resolved before the proposals are implemented. The following should be considered:

- What will amount to "appropriate evidence" GST has been collected?
- How will the proposed solution (providing Customs with appropriate evidence) work in practice? Can evidence be provided by contacting a Customs hotline, via an online portal or will paper-based evidence be required?
- How will refunds of double taxation actually occur? Will the consumer need to provide Customs with their bank account details so the refund can be made electronically? How long will it take Customs to process the refund?
- Would it be possible to have an "approved supplier" system where the Commissioner has the discretion to issue a notice stating that offshore suppliers with good systems and/or good New Zealand compliance history can be assumed to have applied the rules correctly?
- Could the $400 threshold be optional? For example:
    - The vendor must collect GST on goods valued at or below $400, and
    - The vendor may collect GST on goods value above $400, and
    - Customs collects GST at the border if no evidence of vendor collection is provided.

Exchange rate issues

6.6 Page 6 of the IRD memo refers to double taxation, or non-taxation, which may arise when the vendor sells the goods at or below $400, but Customs calculates the value to be above $400. The IRD memo notes that this issue is most likely to occur when goods are priced in a foreign currency which needs to be converted into New Zealand dollars.

6.7 The proposed solution in the IRD memo is for the import entry documentation to list the value in New Zealand dollars based on the conversion rate at the time of supply and possibly also the date of supply to allow Customs to check the correct exchange rate was used.

6.8 Consideration should be given as to whether it is desirable to place additional compliance requirements on Customs when the variances may not be material. In addition, we are unsure whether a special system for New Zealand would be realistic. Instead, if Customs has evidence that GST has been paid, could it be allowed not to enforce the $400 threshold for those goods rather than check exchange rate calculations?

6.9 We also question whether it is necessary to have separate exchange rate rules for goods as compared to services – if time of supply is the only viable choice for goods (as suggested in the IRD memo), then that is what will be used out of the four conversion options.

Reasonable belief exception

6.10 We do not support the adoption in New Zealand of the Australian "reasonable belief" exception referred to at paragraphs 3.20–3.21 of the DD and pages 7-8 of the IRD memo. This test is too subjective and will be difficult for Inland Revenue to enforce. We agree with the IRD memo that there would be a risk suppliers would perceive (or claim) there to be a reasonable belief low-value goods will be sent in a consignment valued above the threshold even when this is not the case.

7 EMPs

EMPs as the default supplier

7.1 Proposed special rules in relation to EMPs are outlined at paragraphs 4.7-4.15 of the DD and pages 1-5 of the IRD memo.

7.2 Paragraph 4.15 of the DD asks for feedback on whether, as a default rule, treating the marketplace as the supplier of the goods provided that any of the conditions in paragraph 4.10 are met is workable. Issues to address include:

- We agree with the comment on page 3 of the IRD memo that it is possible some EMPs may be liable for GST in situations where it may not be reasonable to deem them to be the supplier for GST purposes – such as where they might not have enough information to accurately determine the GST treatment of a supply and account for GST without incurring disproportionate costs. We support the suggestion that EMPs should be able to apply to the Commissioner for an exercise of her discretion if the EMP operator considers it has a compelling case that it cannot reasonably be expected to be able to comply with the requirements.

- We are uncertain as to the scale of the systems challenge for EMPs to collect GST on transactions agreed using the EMP. Each EMP may operate a slightly different platform and, in addition, EMPs could be reluctant to invest scarce systems development and coding expertise in complying with the proposals until the legislation is enacted in its final form.

- There is a risk some EMPs may be reluctant to supply into the New Zealand market as a result of the new rules, similar to the experience in Australia regarding geo-blocking of Australian consumers from overseas websites. A similar response by EMPs to New Zealand's proposed rules would reduce choice for New Zealand consumers.

Scope of the rules

7.3 The potential scope of the proposed rules for EMPs is discussed at pages 4-5 of the IRD memo, with two main options:

(i) Deeming the EMP operator to be the supplier regardless of residency or location of the vendor, or

(ii) Deeming the EMP operator to be the supplier only if the vendor is based outside New Zealand.

Option (i)

7.4 In our view, deeming the EMP operator to be the supplier in relation to supplies made in New Zealand (on which GST is working well) seems unnecessarily complex.

Option (ii)

7.5 In terms of assessing residency should option (ii) be adopted, we question whether using the location of the supplier is an appropriate proxy for the vendor's residency given many New Zealand businesses may have offshore distribution hubs.

7.6 Page 4 of the IRD memo states it might be less costly for the EMP operator to return GST on all supplies of low-value goods to New Zealand consumers, rather than be required to make further changes to their systems so that GST is not applied to goods sold by vendors located in New Zealand. A solution to this issue suggested in the IRD memo is the possibility of allowing EMP operators to agree with vendors who are located in New Zealand that the EMP operator is responsible for GST on supplies made through its marketplace to New Zealand consumers. We do not consider this option to be viable, given that vendors are likely to sell through a range of outlets (such as physical stores, their own website, various EMPs etc.). Such an approach would therefore complicate vendor systems and result in the risk of errors.

7.7 Pages 4-5 of the IRD memo suggest special rules for GST-registered vendors who are located outside New Zealand. In our view, this situation is unlikely to be common enough to warrant special consideration.

Possible carve-out for EMPs through which predominantly domestic supplies are made

7.8 Page 5 of the IRD memo suggests a potential carve-out under options (i) or (ii) for EMPs where the majority of sales of low-value goods to New Zealand consumers through the EMP are made by resident vendors. We do not support this carve-out as it is likely to require complex tracking and assumes an unchanging business model in a fast-moving space.

8 Other matters

Identifying business-to-business supplies

8.1 Paragraph 3.32 of the DD proposes that offshore suppliers would be required to assume a New Zealand consumer is not a GST-registered business unless the customer has communicated to the supplier their GST registration number, New Zealand Business Number or self-certification as a GST-registered business.

8.2 Further consideration should be given to how offshore suppliers can accurately identify GST-registered businesses. For example, should there be an online tool for checking the validity of GST numbers?

Joint registration system

8.3 Paragraphs 5.6-5.9 of the DD refer to the opportunity to explore a joint-registration system with other countries, particularly Australia, in the future.

8.4 While a joint registration/payment system sounds good in theory, we believe such a system is likely to be unworkable in the foreseeable future. It would require a greater alignment of the GST rules and significant technological investment. Concentrating on data matching and information sharing with the Australian Tax Office is likely to provide the Government with a greater return on investment.

We would be happy to discuss any aspect of our submission with you. Please contact me in the first instance in that regard.

Yours sincerely

David Snell

David Snell
Executive Director
Ernst & Young Limited